Asia Now Aerospace Market Brief – Philippines

Section I: Narrative

Despite the increasing cost of fuel, political uncertainty and the weakening peso, the Philippine aerospace industry offers bright prospects for U.S. companies. In fact, total imports of aviation and military spare parts increased by nearly 22% from USD156 million in 2003 to USD191 million in 2004, and industry experts conservatively project an additional 15-20% increase in 2005. Over the past two years, Philippines Airlines (PAL) and Cebu Pacific- the country's two largest carriers- have pursued their re-fleeting programs and expanded domestic and regional routes, maintaining passenger load factors of more than 70%. This means that most of the flights of these two airlines are cost effective and profitable. Furthermore, the entry of smaller airlines such as Tiger Airlines and JetAsia, which offer low cost flights to near-by Asian destinations such as Singapore and Malaysia, has reinvigorated local competition and has been the impetus for infrastructure improvements in airport facilities, particularly at Clark International Airport. From January to September 2005, inbound visitors increased by 12% compared to the same period in 2004 (1.7 million in 2004 to 1.9 million in 2005), in large part due to the Philippine Department of Tourism's WOW (World of Wonders) travel campaign.

The Philippines is home to 85 airports (4 international, 4 alternate international, 12 trunk line, 36 secondary, 29 feeder) and is currently serviced by 37 international airlines, including PAL, Cebu Pacific, Northwest, Cathay Pacific, Singapore Airlines, and Malaysian Airlines, among others. Locations of these airports are shown in the map on the next page. In 2004, more than 15 million passengers passed through the Ninoy Aquino International Airport (NAIA 1 and 2) and regional airports. Manila's NAIA Terminal 2 handles international and domestic flights of the country's flag carrier, PAL, and is the busiest terminal in the country, with a yearly capacity of 10 million passengers. Though complete, NAIA Terminal 3, a 65-hectare airport with a capacity of 10 to 14 million passengers, is as yet not operational due to unresolved legal issues. The Philippine Air Transportation Office (ATO) and the Manila International Airport Authority (MIAA) have jurisdiction over these airports and also make upgrade and equipment purchase decisions for the Ninoy Aquino airports in Manila.

PAL, Cebu Pacific Airlines and Air Philippines are the country's three major airlines, with PAL capturing about 50% of total domestic and international traffic. With 18 domestic and 21 regional destinations, PAL maintains direct flights from Manila to San Francisco, Los Angeles, Hawaii and Las Vegas, and recently opened a direct route to Beijing. The airline currently has 32 aircraft and is planning to complete their re-fleeting expansion by 2008. The company intends to replace part of their aging fleet with long haul, fuel-efficient wide-body aircraft. Domestically, PAL's also offers popular travel packages, such as their marquee PALAKBAYAN packages, which combine low cost domestic fares with hotel accommodations.

Republic of the Philippines
NATIONAL AIRPORTS
LEGEND
INTERNATIONAL 4
ALTERNATE INTERNATIONAL 4
TRUNKLINE 12
SECONDARY 36
FEEDER 23
REGION 1
REGION 2
CAR
LAOAG
REGION 3
CLARK
SUBIC
MANILA
NCR
REGION 5
REGION 4
REGION 8
REGION 6
REGION 7
CEBU
REGION 13
CARAGA
REGION 10
REGION 9
ZAMBOANGA
DAVAO
REGION 11
TAMBLER
REGION 12
ARMM
MAY 2004

Of the Philippine carriers, Cebu Pacific Airline captures about 38-40% of the combined domestic and international traffic. In 2005, the company started their USD670 million re-fleeting program by purchasing 12 new A319s. Delivery started in September 2005 and completion is expected by 2007. Recently, the company signed a joint venture maintenance agreement with SIA Engineering Company Limited (SIAEC), a unit of Singapore Airlines for its new fleet and existing DC9's and B757's. Aviation Services Philippines Inc. (ASPI), the joint venture firm, will provide total airframe support, line maintenance, technical ramp handling service and light maintenance checks to airline customers at the 13 Philippine airports that Cebu flies to. ASPI is currently considering building their maintenance facility at Clark International Airport, Pampanga.

In 2005, Air Philippines' captured less than 15% of the domestic traffic and phased out their six YS11s. As replacements, they leased six B737-200 to fly to their 13 Philippine and four international destinations. The airline maintains a Cebu hub, which flies to 6 destinations in Cebu and Mindanao (southern Philippines). The company has plans to expand their fleet in 2007.

Asian Spirit flies domestically and focuses on vacation travel, particularly to the Boracay resort island. The company owns seven aircraft and leases four (four YS-11 turbo-props, two CN 235's, two Dash-7's and three Let 410's). The company purchased two (2) Dash-7s to eventually replace their YS-11's.

Through the ATO, the government currently has several infrastructure projects open for international competitive bidding. Most projects are financed through foreign government-funded grants, bilateral aid, Japan Bank for International Cooperation (JBIC) programs, the Asian Development Bank and other concessionary financing. Bidding on these projects is often reserved for national firms of the governments that fund the projects. The implementation of these projects will result in the purchase of air traffic control equipment, international landing systems, fire rescue vehicles and maintenance equipment such as sweeper and dump trucks, X-ray machines, baggage handling equipment and systems, cargo handling equipment, airport safety and security equipment and CNS/ATM systems. These projects include:

- New CNS/ATM Development Project
- Nationwide Air Navigation Facilities (ANF) Modernization Project-Phase III
- Rehabilitation of the Manila TRACON Facility Project
- Emilio B. Javier Airport Development Project (Antique Airport)
- Bantayan Airport Development Project (Bantayan Island, Cebu)
- Godofredo P. Ramos Airport Development Project (Caticlan Airport)
- M'Lang Airport Development Project (M'Lang Cotabato)

For complete information about these projects, please visit www.ato.gov.ph, www.dotcmain.gov.ph

Generally, the playing field is most level for U.S. manufacturers as primary bidders in ADB-financed projects, such as the ongoing Third Airport Development Project (see

ADB listing). For JBIC or foreign government funded projects, U.S. firms are typically equipment suppliers or sub-contractors to the pre-qualified bidders who are awarded the contracts. U.S. airport services, program management consultants and suppliers of air navigation, air traffic control facilities, and airport equipment and services usually partner with the pre-qualified bidders and build relationships with the project's proponents. U.S. companies recently active in the market include GE for engines, Honeywell, L-3, Teledyne, Rockwell for avionics, Boeing for aircraft and parts, Northrop Grumman for avionics and other parts, and Goodrich for tires, brakes and wheels. In 2004, U.S. companies captured about 40% of the total market for aviation and related parts and accessories.

Within the commercial and general aviation sub-sector, opportunities exist in the supply of spare parts and accessories to airline operators and accredited repair facilities. Although the market is not large, sales opportunities exist for aircraft precision parts and components, landing gear, engine parts, cabin parts and aviation training and simulation.

In military aviation, market prospects are limited to spare parts for C130's, UH-IH's and MG-520's, as well as limited upgrading of existing aircraft. Because of budget constraints, the Philippine Airforce Modernization program has not been fully implemented.

The Department of Transportation and Communications (DOTC) is the Government's over-arching transportation sector policy planning department. Within DOTC, ATO prescribes rules and regulations for the inspection and registration of all aircraft owned and operated in the Philippines and for all air facilities. ATO also establishes and prescribes corresponding rules and regulations for the enforcement of laws governing air transportation and determines, fixes and/or prescribes rates pertinent to the operation of public air utility facilities. The Office also offers support operation services to national airports and air navigation facilities, as well assistance in complying with ICAO. MIAA performs this function for the NAIA terminals.

By contrast, the Civil Aviation Board regulates the economic aspects of air transportation, such as licensing of domestic and international airlines and regulating the fares and rates for the transport of persons and property. The Board also participates in the negotiation of air agreements covering exchange of rights.

Aviation and aerospace related equipment and accessories are freely importable into the Philippines with duty charges ranging from three to five percent. The Bureau of Customs is responsible for monitoring and inspecting all imported goods. The Philippines also imposes a 12% expanded value-added sales tax (eVAT) on all goods sold within the country. The full burden of the VAT typically falls on the end buyer.

While foreign suppliers can import directly, it is common practice to designate a local distributor and/or value-added reseller. The market expects foreign players to develop a technical support site in the country. Technology transfer and regular training of local staff or partners is expected.

The Philippines is a price sensitive market, and corporate customers and consumers alike expect discount pricing and price packages tailored to different levels of affordability. For instance, it is rumored that Airbus won the recent Cebu Pacific re-fleeting bid by offering a financing package more attractive/flexible than Boeing's. Also, relationship building is crucial in the Philippine market; therefore expect to allocate a large share of marketing funds to sales representation and account management.

Since major aviation projects require considerable capital expenditures, it is common practice for equipment suppliers to arrange financing. Financing tends to be arranged through a combination of loan packages from foreign banks and export credit agencies or raised directly through the money markets. Equipment suppliers play a key role in securing necessary financing.

Section II: Specific Questions from ODO Clients

1. What are the prospects for general aviation aircraft (business jets, turboprops and piston aircraft) in your country?

   Despite the increasing fuel costs and uncertainty in the Philippine political environment, major airlines such as PAL, project that the general aviation market will grow by 2-3% in 2006. Though prospects are modest, airlines are in a re-fleeting mode and sales of spare parts, avionics and maintenance services are expected to increase over the next three years.

2. Overview of who has jurisdiction within Government, and allocated budget? Break down of how aerospace funds are spent.

   The Department of Transportation and Communications (DOTC) has the overall jurisdiction over the transportation sector. They are also responsible for the allocation of the Government budget for the aviation sector. A complete breakdown of aerospace funds is not available. Please contact CS Manila for individual contacts within the DOTC and other relevant government agencies.

3. Overview of Military and Civil fleet – Type of planes, Age of planes – Cargo and Passenger.

   Because of funding constraints, the implementation of the Armed Forces of the Philippines Modernization Project (AFPMP) is still incomplete. The military has redirected its priorities to upgrading existing aircraft in place of new acquisitions. It is expected that the current inventory of Philippine Air Force assets will continue to shrink in the absence of acquisitions of new aircraft. The PAF proposal is limited to medium and light transport package which includes the upgrading of C-130 Hercules transport aircraft, F-27 Fokker aircraft and the upgrade of UH-1H Huey helicopters. It also includes the upgrade of F-5 A/B Fighters and S-76 helicopters.

4. Does the country have companies that rebuild planes/retrofit for companies?

   Generally none. Sometimes, Lufthansa Technik, the maintenance facility for PAL, does simple retrofit work for PAL planes' interiors such as upholstery repair or complete interior change. Other than this, the company does repair and maintenance work for PAL and their other clientele.

5. Do aerospace companies inventory parts, or contract with companies to supply parts on demand? If so, who are these types of companies?

   Generally aerospace companies do not maintain high-level parts inventories. They send their aircraft to repair facilities in the region. Lufthansa Technik Philippines, a joint venture between Macroasia and Lufthansa Technik of Germany provides maintenance service to Philippine Airlines. The company is engaged in aircraft maintenance, repair and overhaul, and has maintenance contracts with Air Mauritius, Austrian Airlines, and a few smaller airlines flying into Manila airport. The company also handles the overhaul of Lufthansa's A340 and A330 airplanes. Lufthansa maintains spare parts and avionics equipment for their clientele.

   Recently, Cebu Pacific Airlines, the second largest Philippine carrier, signed a joint venture agreement with SIA Engineering Company Limited (SIAEC), a unit of Singapore Airlines, for the maintenance of their new Airbus aircraft and existing fleet DC9's and B757's. Aviation Services Philippines Inc., the joint venture firm, will provide total airframe support, line maintenance, technical ramp handling services and light maintenance checks such as "A" checks to airline customers at 13 Philippine airports serviced by Cebu Pacific. The company is considering establishing their facility at Clark International Airport, Pampanga.

6. Is the airport public/private? – Do they require local partners to bid on contracts?

   The Manila International Airport Authority (MIAA) maintains and manages the operations of the NAIA terminals. The Air Transportation Office (ATO) operates and maintains national airports, air navigation and other similar facilities in compliance with ICAO. It is not a requirement for foreign companies to partner with local firms to bid on internationally bidded projects. However, partnering with Philippine firms usually is the most effective way to do business in the country. The local partner becomes the in-country market link, who can regularly monitor the project and liaise with the implementing agencies.

7. Do they generally lease or buy aircraft?

   Airlines both lease and buy aircraft. Below is the list of airlines with their fleet:

   - **Philippine Airlines (PAL)**

Total: 32 aircraft (2 Owned, 19 Financial lease, and the remaining standard lease)

Owned:
King Air (1)
B737-300 (1)
Financial lease (PAL will eventually own after 15 years)
B747-400 (4)
A340-300 (4)
A330-300 (8)
A320-300 (3)
Standard Lease
B747-400 (1)
B737-300 (3)
B737-400 (3)
A320-300 (4)

- **Cebu Pacific**

  Total: 15 aircraft (13 Owned and 2 Leased)

  Owned
  DC9 (9) but will be phased out by 2007 and replaced by A319/320
  A319 (4)
  Lease
  A320-300 (2)

- **Air Philippines**

  Total: 6 aircraft (B737-200 and all leased)

- **Asian Spirit:**

  Total: 11 aircraft (7 owned and 4 leased)

  Owned:
  YS-11 turbo-prop (4)
  Let 410 (3)

  Leased
  CN 235 (2),
  Dash7 (2)

8. What is the best way to find out about government bids in the market?
   What regulations are there, if any, on selling used equipment into the market?

All the projects of the DOTC (www.dotcmain.gov.ph), ATO (www.ato.gov.ph), MIAA (www.miaa.gov.ph) and Philippine Air Force (www.paf.mil.ph) are posted on their respective websites. ADB-financed projects are also available on their website (www.adb.org).

Used aviation and aerospace related equipment and accessories are freely importable with duty charges ranging from 3% to 5%. The Bureau of Customs is responsible for monitoring and inspecting all imported goods. The Philippines also imposes a 12% expanded value-added sales tax (eVAT) to all goods sold within the country.

Section III: Regional Aerospace & Defense Event(s)

Asian Aerospace 2006

Asian Aerospace in Singapore is one of the world's premier aerospace and defense technology events. Encompassing all civil and military sectors of the international aerospace industry, Asian Aerospace is the foremost platform for companies to showcase their products and services in the Asia-Pacific region. In 2004, the show attracted 759 exhibitors from 37 countries, and 26,814 visitors from 81 different countries.

U.S. Department of Commerce, U.S. Commercial Service, Aerospace & Defense Team Programs and Services at Asian Aerospace 2006

The U.S. Department of Commerce is pleased to bring to your attention to three powerful opportunities to participate in at Asian Aerospace 2006. We are organizing/supporting programs for U.S. companies exhibiting, attending or just wanting a presence at the show. Please review the following for more information on the U.S. International Pavilion, Aerospace Executive Service and the Aerospace Product Literature Center:

- **EXHIBIT IN THE U.S. INTERNATIONAL PAVILION** through our official national pavilion organizer Reed Exhibition. Exhibiting packages start at approximately $5,000 - please contact Ms. Sarala Govindan at (203) 840-5355 or sgovindan@reedexpo.com for more information.

- **AEROSPACE EXECUTIVE SERVICE:** The Aerospace Executive Service (AES) is best suited to small- and medium-sized U.S. businesses attending Asian Aerospace 2006 with the goal of making business appointments, generating sales leads, and developing sales channels. The service will include two days of pre-screened business appointments on February 20-21, 2006 and an AES booth for product literature display at exhibition. The cost to participate is $3,000 plus $700 for each additional person from the same company. Contact either Eric Nielsen (tel 520-670-5540 / eric.nielsen@mail.doc.gov) or Amy Magat (tel 213-894-3966 / amy.magat@mail.doc.gov) for more details.

- **AEROSPACE PRODUCT LITERATURE CENTER:** The Aerospace Product Literature Center is targeted to businesses that either will not attend the show, or would like to supplement their presence with an additional method of promoting their goods and services. For the low cost $650, the U.S. Commercial Service will display your company literature in a special booth. For more information about the APLC, please contact Deborah Semb at 202-482-0677 or email her at Deborah.Semb@mail.doc.gov.

Section IV: Local Aerospace & Defense Event

None

Section V: Post's contact information

Brent E. Omdahl, Commercial Attaché
brent.omdahl@mail.doc.gov

Aida Lescano-Miranda, Sr. Commercial Specialist
aida.miranda@mail.doc.gov

25th Floor, Ayala-Life FGU Bldg., 6811 Ayala Avenue, Makati
Tel: (632) 888-4088, Fax: (632) 888-6696
Email: Manila.Office.Box@mail.doc.gov